

Bachus Letter to SEC Chairman Cox

July 19, 2007

House Financial Services Ranking Member Spencer Bachus (AL) sent the following letter to Securities and Exchange Commission Chairman Christopher Cox.

July 10, 2007

The Honorable Christopher Cox

Chairman

Securities and Exchange Commission

100 F Street, NE

Washington, DC 20549

Dear Chairman Cox:

I am writing to urge the Securities and Exchange Commission's ("SEC" or "Commission") prompt attention to an issue arising out of the decision by the United States Court of Appeals for the District of Columbia in *Financial Planning Association v. SEC* ("FPA"). As you know, the court in FPA vacated a 2005 SEC rule exempting from the requirements of the Investment Advisers Act of 1940 broker-dealers that receive fee-based compensation and provide investment advice that is "solely incidental" to the broker-dealer's brokerage services. The court's ruling has placed into legal jeopardy more than one million brokerage accounts, and could fundamentally alter the relationship between investors and brokers.

Financial markets require regulatory clarity and certainty. However, the Court in FPA has overturned years of established

business practices between brokers and consumers, making it incumbent upon the SEC to ease the transition to a new regime. Regulatory inaction in this instance is, in my view, inconsistent with the goal of assuring that the U.S. capital markets remain the most efficient and competitive in the world based on their responsiveness to investor needs and protection of investor choice.

As you know, fee-based brokerage grew out of the 1995 SEC-sponsored Tully Commission Report, which found that this form of compensation better aligned the interests of brokers and consumers than commission-based brokerage. There are at least one million consumers who have chosen to put \$300 billion in fee-based brokerage accounts, and nearly half of these are being held by customers as retirement accounts. Since 2005, the broker-dealer industry has reasonably relied on SEC Rule 202, and prior to that a 1999 no-action letter issued by the Commission, to permit the use of asset-based compensation. The industry had nine months to implement the rule when it was passed, and it largely reflected existing practice. Responding to a reversal of this long-standing policy is a much greater task, and it appears that the industry will have far less time to come into compliance than it did when fee-based commission arrangements were first authorized. Unless the SEC intervenes, there will not be time for an orderly transition in which customers of broker-dealers are adequately informed about the changes caused by the FPA opinion and their alternatives.

Firms cannot simply "convert" their clients' brokerage accounts into investment advisory relationships. Investment advisory and brokerage services are separate and distinct and each is governed by different laws, regulations and duties. Investment advisory relationships can only be created after all the necessary and appropriate discussions with clients have occurred, and of course, the clients' affirmative agreement must be obtained. Further, only upon that agreement can all the required profiling, selection process and documentation start to occur.

While I fully support your decision to approve additional emergency funding to accelerate the RAND Corporation study of the marketing, sale, and delivery of financial products and services to investors in this area, the Commission should not wait until the study's expected December release. Instead it should provide brokerage customers and providers the certainty they require to continue their chosen financial relationships.

Thank you for your consideration. I look forward to your response.

Sincerely,

Spencer Bachus

Ranking Member

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